

## **SECTION 1:**

### **Changes in tax law may affect your employees**

What you need to know about **IRS Notice 2006-110** "Recordkeeping Requirements for Charitable Contributions made by Payroll Deduction" and the **Pension Protection Act of 2006**:

- ❑ These new rules apply to contributions "made in taxable years beginning after August 17, 2006". For most individuals (like employees) who go by calendar year for taxes, these new tax rules went into effect for contributions made starting January 1, 2007 and thus for taxes filed in April 2008 covering the January — December 2007 tax year.
- ❑ If an employee makes a charitable contribution of cash, a check, or other monetary gift, to claim an income tax deduction, the employee must have a bank record (cancelled check, bank or credit card statement) **OR** written acknowledgement from a charitable organization showing the date, amount contributed, and name of the organization.
- ❑ If your employees contribute to charity through payroll deductions, the IRS says that the substantiation requirements will be considered to be satisfied if each of your employees has a pay stub, W-2 or other employer document showing the total amount withheld for the charitable organization **AND** a donor pledge card (the original, a carbon copy or a photocopy of a paper form, or a printout of an online donation). This is needed to substantiate and claim a tax deduction. A letter prepared by or at the direction of the charity (stating the date, amount donated, and "no goods or services language") also qualifies. (*\*See sample tax statement below for language that needs to be included on the pledge form.*)
- ❑ Donors are now required to have an official record or written communication from the charity, or from an employer at the direction of the charity, to substantiate any contribution for tax purposes. Companies and charities can help:
  - o Companies can add a statement to their online pledging system and ask employees to print a copy. (*\*See sample tax statement below.*)
  - o Companies can retain and archive the original pledge card or a copy of the pledge card to provide a copy to employees at tax time.
  - o Companies can provide donor-level pledge information to local United Ways so they can provide acknowledgements. Any acknowledgement must include the name of the charitable organization, date of donation and amount donated. [Note: Under prior law, donors were required to obtain acknowledgements for any donation in excess of \$250 (or for payroll deductions, \$250 per pay period). Under the new law, donors are required to have an acknowledgement for all donations. The only difference is the "no goods or services" language is not required on donations less than \$250.] United Way should work with all donors to provide acknowledgments. If a local United Way does not have detailed donor information, United Way will need to contact the company campaign coordinator to obtain that detail so a charitable contribution acknowledgment letter can be provided or to arrange for the donor to receive a copy of the pledge card from the company.
- ❑ Under the prior law, donors could use "other reliable written records" to substantiate charitable contributions for tax purposes. The difference now is that the IRS is being specific about what official documents will be accepted as proof of charitable contributions, which may lead to increased enforcement by tax preparers and auditors.

#### **Sample tax statement for e-Pledging:**

Since a pledge card or other document "prepared by or at the direction of" the charitable organization meets IRS Notice 2006-110 rules, we suggest your e-pledging system automatically generate this acknowledgement for your employees:

*[Date] Thank you for your pledge of [total \$ amount] through the United Way campaign. No goods or services were provided in exchange for this contribution. Please print this acknowledgement and keep it for your tax records. You will also need a copy of your pay stub, W-2 or other employer*

*document showing the amount withheld and paid to a charitable organization. **Consult your tax advisor for more information.***

Companies may also want to include the "no goods or services" line on pledge cards.

#### Sources:

- IRS Notice 2006-110 "Recordkeeping Requirements for Charitable Contributions made by Payroll Deduction"
- Calls with author of IRS Notice 2006-110, Nancy J. Lee, Office of Associate Chief Counsel (Income Tax & Accounting), 1/12/07, 1/16/07, 3/2/07, 3/13/07, phone #202-622-5020
- IR-2006-186, "New Guidelines for Payroll Deduction Contributions to Charities"  
<http://www.irs.gov/newsroom/article/o,,id=16463o,00.html>
- IR-2006-192 "Recent Tax Law Changes May Affect People Giving to Charity: IRS Offers Tips for Year-End Donations" December 14, 2006
- IRS Publication 1771 (Rev. 3-2002)
- Calls with IRS agents 1/11/07 (specifically agents Mr. Carter, #1921302; Mr. McKennon, #5908060; and Mr. Holland, #17-19561), phone #1-800-829-1040
- "New IRS rules demand receipts for church donations," by Jeff Diamant, Chicago Tribune, Published January 8, 2007
- Ken Euwema, UWA Vice President of Membership Accountability, phone #703-836-7112 (x565)

## SECTION 2

### Q&A

#### 1. What about special event fundraisers (collecting cash for jeans day, office raffles, bazaar purchases, auctions, bake sales, etc. to fund raise for charity)?

In general, raffles are not tax deductible. Additionally, many common fundraising activities (see IR 88-120) are questionable and only borderline acceptable since they do not qualify for the "*No goods or services were provided in exchange for this contribution*" stipulation. If employees want a tax deduction, they must have an acknowledgment or other acceptable substantiation documentation. A company can provide an acknowledgment stating what the employee paid for and the date; however, the onus is on employees to determine tax deductibility with their tax advisor (issues: substantial value, intangible benefits, gift, fair market value, etc.)

#### 2. Can a for-profit online pledging/processing company provide charitable acknowledgment letters?

Yes. An e-pledging/processing company that collects and distributes donations to charity can receive donations as well as provide written acknowledgment of those donations for tax purposes. (See Rev. Rut. 2002-67)

#### 3. How do companies acknowledge continuous/rollover givers if donors sign up once and keep giving every year, but do not receive a new pledge card?

Under the new law and published IRS guidance, continuous/rollover givers must obtain and retain the same documentation as other taxpayers to substantiate donations for tax purposes, such as a pledge card and Form W-2, OR an official bank record. If the pledge card indicates the donation is ongoing, employees should be able to use the same card as long as it matches the W-2. (If pledge card says employee will give 2% and W-2 withholding can be calculated to show 2%, the same pledge card is fine.) If continuous givers do not currently have a pledge card, a company could provide a printable statement with the date, amount pledged, charity and "no goods or services" language.

#### 4. How can charities acknowledge anonymous givers?

A charity cannot acknowledge donations for tax purposes unless it receives detailed donor information. If a company wants the charity to provide acknowledgments for employees, the company must release the employee information. If the company does not want to provide employee information to the charity but still wants to ensure that employees can substantiate their donations for tax purposes, the company would be responsible to provide that acknowledgement prepared by or at the direction of the charity, using the language below. Or, employees could pay their charitable donation by check and use an "official bank record" as substantiation, thus removing the need for acknowledgement from a charity.

*[Date] Thank you for your contribution of [total \$ amount] through the United Way campaign. No goods or services were provided in exchange for this contribution. Please print this acknowledgement and keep it for your tax records. You will also need a copy of your pay stub, W-2 or other employer document showing the amount withheld and paid to a charitable organization. **Consult your tax advisor for more information.***

#### 5. What options can a donor use to substantiate a charitable contribution?

Donors have at least three options to substantiate charitable contributions for tax purposes:

- ☐ **Cancelled check** or other official bank record (law now permits **bank and credit card statements**)
- ☐ **Written communication from the charity** with the date, amount donated and "no goods or services" language (ex.: a letter provided by United Way)
- ☐ In the case of **payroll deductions**, a **Form W-2**, pay stub or other official employer document showing the charitable withholding **AND** one of these: an original **pledge card**, carbon copy of a pledge card, photocopy of a pledge card, tear-off receipt from a pledge card, printout of an online pledge card, or a printed statement prepared by or at the direction of a charitable organization that acknowledges the date, donation amount and name of the charity.

*Note: "Other reliable records" no longer qualify as acceptable substantiation.  
Source: internal Revenue Code Section 170 and Notice 2006-110*

If donors follow IRS Notice 2006-110 and provide the above documentation, they will be in compliance with the law (considered "safe harbor"). If the above is not followed, donors still may be able to deduct their charitable contributions but should consult their tax advisor.

For cash contributions, it is recommended that the acknowledgment be signed and dated by an authorized representative of the charity.

#### 6. Some 2006 campaigns occurred before this new law (August 2006) and Notice 2006-zso (December 2006). Do we still have to receipt donors since the opportunity has passed?

Unfortunately, the law requires either an official bank record or written substantiation from the charity. For payroll deductions, a pledge card issued at the direction of the charitable organization in addition to a W-2 will satisfy the law. To meet these requirements, a company can re-issue pledge cards or provide an email receipt, or a company might consider releasing donor information to the charitable organization so they can provide acknowledgements to employees.

#### 7. Is it true employees only need a charitable acknowledgement if they itemize their tax deductions?

Yes. If employees do not itemize their deductions, they are not even permitted to take a charitable contribution deduction. More than half of Americans take the standard deduction, so they will not need a charitable acknowledgement or receipt of any kind. However, most homeowners, who usually itemize, will.

#### 8. What if I need more information or need an answer officially verified?

First, talk with your corporate accountants and general counsel. Second, consider calling the authors of IRS Notice 2006-110 "Recordkeeping Requirements for Charitable Contributions Made by Payroll Deduction"

Nancy J. Lee and Patricia M. Zweibel of the Office of Associate Chief Counsel (Income Tax & Accounting), who welcome specific questions regarding the notice at #202-622-5020. However, to receive a binding decision from the IRS on a specific tax issue, a company must submit an IRS Ruling Request. Since the Pension Protection Act of 2006 (August 17, 2006) and IRS Notice 2006-110 (December 2006) are relatively new laws and further guidance may be pending, the IRS may be unable to issue a ruling request on these topics.

#### Sources:

- Calls 2/20/07, 2/21/07, 3/2/07 and 3/13/07 with Nancy J. Lee, author of IRS Notice 2006-110, Office of Associate Chief Counsel (Income Tax & Accounting), phone #202-622-5020
- Information Release 88-120 OR 88-120; 1988 IRB LEXIS 3836; January 1, 1988, August 4, 1988)

### **SECTION 3**

#### **Additional Q & A**

##### **1. Why does an employee need a pledge card?**

The rationale behind requiring a pledge card for tax purposes is because the vast majority of pay stubs and W-2 forms that show the withholding do not also show the name of the charity. The IRS needs to be able to match the name of the charity with the amount given to the charity to verify tax deductibility.

##### **2. What if an employee stops payroll deductions during the year? The pledge card will not match the final amount withheld on the form W-2.**

It is recommended that employees save both their pay stubs and Form W-2. Pay stubs should suffice since the pledge card should say \$20 per pay period will be withheld, and the pay stubs would indicate that withholding. If an employee only has the Form W-2 but the amount withheld for charity on the W-2 is less than the amount pledged on the pledge card, the W-2 will likely qualify as substantiation for the lesser amount. Employees should consult their tax advisor for more information.

##### **3. What if an employee pledges a percent of pay and receives a raise during the year? The pledge card percent and the Form W-2 amount withheld may not match up.**

Even if an employee receives a raise during the year, the year-to-date compensation on the final pay stub, as well as on the Form W-2, should still match the pledge card. The Form W-2 shows the actual amount earned that year, not the employee's annual salary, so the percent on the pledge card should match the percent withheld for charity from the actual amount earned.

##### **4. What if a company runs a campaign from March to March (instead of January 1 through Dec. 31)? The withholding on the Form W-2 is not going to match the pledge card.**

The Form W-2 for taxpayers has always run on a calendar year (January 1 through December 31). In this case, that calendar year will overlap two campaign periods and two pledge cards. The employee should retain both pledge cards that overlap the calendar year. Although it might be challenging to calculate, if audited, the employee will be able to match the amount withheld on the form W-2 with the two pledge cards.

##### **5. If a company acknowledges the amount of the prior year's gift on the employee's new pledge card, can the pledge card be used for both the current year pledge and the prior year pledge?**

Yes. The pledge card would be valid for two years since it would recognize the amount pledged in the previous campaign which is currently being withheld as well as the amount pledged for the next year. But, to qualify as substantiation for the earlier year, the new pledge card would have to be received by the employee before he files his income tax return for the earlier year.

**6. If an employer, at the request of United Way, provides to each participant in a work place campaign the following information on a year-end pay stub, will both the charity and employer be in compliance with sections 170(f)(8) and (17), as interpreted by IRS Notice 2006-110?**

*Thank you for your contribution/pledge of (total \$ ) for the year 200( ) through the United Way campaign, of which \$ has been withheld from your compensation and paid to the United Way. No goods or services were provided in exchange for this contribution. Please print this acknowledgment and keep it for your tax records. Consult your tax advisor for more information.*

The IRS has not issued any further guidance on this matter since Notice 2006-110 in December 2006, so we are not in a position to provide a definitive answer. However we do believe the following information may be helpful to organizations seeking to comply with the new substantiation requirements.

UWA's outside Washington tax counsel has discussed this with IRS employees who were involved in drafting the December 2006 interim guidance and are involved in determining what additional guidance will be issued in the future. It is clear that in drafting the December 2006 interim guidance, the IRS representatives had envisioned the preparation of two separate pieces of paper, as is reflected in some of the questions and answers, above. However, the IRS employees did not state that an alternative reading is impossible or clearly inconsistent with the December 2006 interim guidance, and they agreed to consider a suggestion to issue future guidance that explicitly approves the use of a single document that contains all of the required information to satisfy the substantiation requirements of the new law. Further, they noted that the December 2006 interim guidance contains reliance language that states specifically that—

*Taxpayers making charitable contributions by payroll deduction may rely on this notice to comply with the new requirements until those regulations are effective.*

Given the goal of the 2006 law change – i.e., to require the creation of documentation of all charitable contributions, showing both the amount(s) contributed and the names of the donee charity(ies) – UWA's outside Washington counsel believes that the IRS would not challenge a taxpayer's good faith interpretation of the December 2006 interim guidance that all of the necessary information can be provided at the direction of a donee charity by an employer to an employee on a single piece of paper. This interpretation appears to be supported by the taxpayer reliance language contained in the December 2006 interim guidance.

Please note that this is provided as information only and is not intended as tax advice by either UWA or its counsel. You are encouraged to consult your own tax advisors or experts.

**Sources:**

- 3/5/07, 3/6/07 and 3/13/07 calls with Nancy J. Lee
- Internal Revenue Code Section 170 and Notice 2006-110